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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934. No. 394.

COMMONWEALTH OF PENNSYLVANIA,
Petitioner,

v.

JOHN G. WILLIAMS, JOSEPH B. SIMON, and CHARLES DENBY, Jr., Receivers of MORTGAGE BUILDING AND LOAN ASSOCIATION.

BRIEF FOR RESPONDENTS.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

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IN THE

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OCTOBER TERM, 1934. No. 394.

Commonwealth of Pennsylvania,
Petitioner,

v.

John G. Williams, Joseph B. Simon, and Charles Denby, Jr.,
Receivers of Mortgage Building and Loan Association.

BRIEF FOR RESPONDENTS.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

This case comes before the Court on Writ of Certiorari issued to review a decree of the Circuit Court of Appeals for the Third Circuit.

OPINIONS BELOW.

The opinion of the District Court for the Eastern District of Pennsylvania, delivered by Judge Welsh on June 17, 1933, is reported as *Elson* v. *Mortgage Bldg. & Loan Assn.*, 1 F. Supp. 779.

The opinion of the Circuit Court of Appeals for the Third Circuit, delivered by Judge Davis on July 24, 1934, is reported as *Commonwealth of Pennsylvania* v. *Williams, et al*, 72 F. (2d) 509.

COUNTER-STATEMENT OF CASE.

The facts appearing in the Petition for Writ of Certiorari and in petitioner's Brief so inadequately present the statement of the case, that a succinct and accurate counter-statement is essential.

Mortgage Building and Loan Association was created on April 7, 1931, by the merger and consolidation of seven associations (R. 20-1). As early as June 5, 1931, within two months after this merger, the Department of Banking summoned the officers of the association for a hearing before it. At that hearing the Department found the association to be in an unsafe and unsound condition (R. 21). Thereupon, on the same day, the Secretary of Banking addressed a letter to the president of the association, referring to the hearing and stating:

> ". . . We gave certain instructions as to how the association is to be operated in the future, which instructions we feel if strictly adhered to will be for the best interest of the stockholders and may work out its salvation.
>
> "The instructions are as follows:
>
> [Here follow the instructions or recommendations.]
>
> . . . . . .
>
> "The above instructions are to be strictly adhered to until the association is again examined by this Department, which will be sometime after the first of the year." (—a period of at least seven months) (R. 28-31).

The Secretary of Banking therefore knew on June 5, 1931, that the association was in an unsafe and unsound condition; he knew for sometime prior to December 6, 1932 (Exhibit "B" of Petition, R. 31 *et seq.*) that the association was insolvent.

In the face of these facts, the almost total want of reference in petitioner's Brief to the claim of Nice Ball Bearing Company is of striking significance. It is that claim which gave rise to the receivership and was its motivating cause. The Bill of Complaint (Paragraphs 17-19, R. 10-11), as well as the Answer to the Petition (R. 39), show that the Secretary of Banking, through his agent, the Chief of the Bureau of Building and Loan Associations, knew that the filing of the Bill of Complaint in this case was imminent and that the solicitor and real estate advisor conferred with the officials of the Department, advising them that liquidation was inevitable and the Department should take possession.

The Record shows that the Bill of Complaint was filed solely because a dissenting shareholder, Nice Ball Bearing Company, had obtained a judgment against the association on May 7, 1932, for $40,044, and that this judgment had been affirmed on appeal on January 16, 1933, by the Supreme Court of Pennsylvania (Reported as *Nice Ball Bearing Co.* v. *Mortgage Building and Loan Association, 310 Pa. 560, 166 A. 239 (1933)).*

Nice Ball Bearing Company was threatening and was about to issue execution whereby it would obtain a preference over all other shareholders, including the plaintiff, who also was a dissenting shareholder and who had paid in to the association as dues the total sum of $31,200. This preference, so sought to be obtained by Nice Ball Bearing Company, was only to be avoided by the application for receivers, which was made in this case (R. 11, 39). Once execution had issued in favor of Nice Ball Bearing Company, it would have obtained an unshakable lien on the property levied upon, for the amendment to the bankruptcy law exempts building and loan associations

from its operation (Act of February 11, 1932, c.38, 47 Stat. 47). What would have happened if the receivership had not been effected upon plaintiff's Bill appears from a subsequent proceeding referred to in the Opinion of the Circuit Court of Appeals (R. 78-9). After the receivership Nice Ball Bearing Company filed a petition seeking to have the receivers turn over to it United States Liberty Bonds in excess of $40,000, which had been placed in escrow by the association at the time of its appeal to the Supreme Court of Pennsylvania from the judgment of Nice Ball Bearing Company. The Circuit Court of Appeals sustained the action of the District Court in refusing a peremptory order to turn over the bonds (see *Nice Ball Bearing Co.* v. *Williams, et al., 66 F. (2d) 881 (1933)).*

Accordingly, the Bill of Complaint was filed more than three weeks after the affirmance by the Supreme Court of Pennsylvania of the judgment obtained by Nice Ball Bearing Company. During all this time the state officials took no steps to bring the association under the jurisdiction of the Department of Banking, although they had been requested to do so. Then only was the Bill of Complaint filed.

Temporary receivers were not appointed without notice of any kind. The decree of the District Judge appointing Temporary Receivers (R. 13), itself recites:

> ". . . Notice of said application having been given to the attorney for the Mortgage Building and Loan Association, and Joseph H. Sundheim, Esq., appearing and not objecting to said appointment of temporary receivers. . . ."

It is conceded that the Bill was filed, the receivers appointed and all the property of the association taken into their actual custody before the Secretary of Banking held his hearing preliminary to the filing of his certificate of possession.

Some improper inference is sought to be created with respect to the identity of one of the receivers, and one of counsel

(Petitioner's Brief, pp. 5-6). One of the receivers named, Mr. Williams, had been designated by the association as real estate officer pursuant to the letter of the Department of June 5, 1931, which required approval by the Department of such choice. He had had no previous connection with the association. Messrs. Simon and Denby were complete strangers to the association at the time of their appointment as receivers. No assertion has ever been made to the District Judge appointing the receivers of any disqualification of the officers acting under its decree.

It is true the District Court refused leave to the Commonwealth to intervene and dismissed its Petition, but it is to be noticed that the one Petition went also to the substance of the present proceeding. Indeed, the present proceeding is based upon that Petition. The District Judge and the Circuit Court of Appeals alike refused leave to intervene only because they considered the petitioner as having already intervened and disposed of its Petition upon its merits. As said by the District Judge:

> "Upon consideration of the whole record, we are of the opinion that no sufficient grounds have been shown to vacate the Court's appointment of the receivership, and since this is the only purpose for which the petition to intervene has been filed, the petition filed by the Attorney General is dismissed" (R. 58).

Indeed, petitioner received more than it was entitled to at the hands of both Courts. For as pointed out by the District Judge (R. 45-6), the Commonwealth of Pennsylvania was not the proper party and the Petition should have been brought by Richard Ennis, Special Deputy Secretary of Banking, appointed by the Secretary to take possession of the association. These procedural questions were waived, however, by the receivers, and both Courts, as the Opinions show, considered the Petition upon its merits.

QUESTIONS PRESENTED.

1. Is the fact that the defendant in a bill for receivership is a building and loan association, in law an ouster of the general jurisdiction of Federal Courts of equity?

2. Is it an abuse of discretion for a Federal Court, admittedly having jurisdiction, to appoint receivers of an insolvent building and loan association, where another shareholder has obtained judgment in a large sum and is about to issue execution whereby he will secure a preference over other shareholders and even creditors, and the State Secretary of Banking, with knowledge of these facts, has failed to take possession, by which he might have prevented the institution of suits and the issuance of executions?

ARGUMENT.

SUMMARY.

POINT I—THE DISTRICT COURT HAD JURISDICTION TO APPOINT RECEIVERS TO LIQUIDATE THE ASSOCIATION.

(a) *The Position of Petitioner in the Court Below.*

(b) *The Source of Equity Jurisdiction of the District Courts.*

(c) *The Equity Jurisdiction of District Courts is not Curtailed in Cases Involving Building and Loan Associations.*

(d) *The Contract of Subscription does Not Impair Federal Jurisdiction.*

POINT II—THERE WAS NO ABUSE OF DISCRETION IN THE APPOINTMENT OF RECEIVERS.

(a) *The Secretary of Banking was Not Exercising Jurisdiction over the Association.*

(b) *The District Court was Compelled to Exercise its Jurisdiction to Appoint Receivers.*

POINT III—CONCLUSION.

POINT I.

THE DISTRICT COURT HAD JURISDICTION TO APPOINT RECEIVERS TO LIQUIDATE THE ASSOCIATION.

(a) *The Position of Petitioner in the Court Below.*

It is argued by petitioner that the District Court is without jurisdiction to appoint receivers to liquidate a building and loan association. This argument is but feebly pressed here. Indeed, the Opinion of the Circuit Court of Appeals reveals that the petitioner there conceded that the Court had jurisdiction and limited its attack to the *exercise* of jurisdiction as an *abuse of discretion.* Circuit Judge Davis said:

> "The Attorney General . . . virtually admits that the District Court did have jurisdiction, but ought not to have exercised it, for he says: 'We are urging, not that the District Court was technically without jurisdiction, but that it ought not to have exercised its jurisdiction'." (R. 77-8)

Having failed to press want of jurisdiction in the Court below, it comes with ill grace for petitioner to advance it, however formally, in this Court. The universal principle which requires fairness to Courts below, is recognized in this Court as well as in Pennsylvania, and it is held that a litigant may not change his theory upon appeal.

> *Texas and Pacific Railway Company* v. *Abilene Cotton and Oil Company, 204 U. S. 426 (1907),*
> *Consolidated Cigar Corp.* v. *Corbin, 285 Pa. 273, 132 A. 364 (1926).*

We shall, however, note briefly the jurisdictional authority of the District Court to appoint receivers of a building and loan association.

(b) *The Source of Equity Jurisdiction of the District Courts.*

The jurisdiction of the Federal Courts is derived from Article III, Section 2 of the Constitution of the United States, which provides:

> "The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, [and] the Laws of the United States . . . ;—to Controversies . . . between citizens of different States . . ."

Congress has executed this organic law by establishing District Courts and by Section 24 of the Judicial Code (28 U. S. C. A. 41 (1)) has conferred upon them original jurisdiction:

> "First, Of all suits of a civil nature, at common law or in equity, . . . where the matter in controversy exceeds, exclusive of interest and costs, the sum or value of $3,000, and . . . is between citizens of different States . . ."

On this broad and comprehensive foundation rests the equity jurisdiction of Federal Courts. Within the range of this broad grant of power is clearly comprehended the jurisdiction exercised by the District Court in this case. Unless there be found elsewhere some plain limitation upon this power, the petitioner's argument must necessarily fall.

(c) *The Equity Jurisdiction of District Courts is not Curtailed in Cases Involving Building and Loan Associations.*

We read petitioner's Brief in vain to find a single final authority, statutory or judicial, in which the unlimited jurisdiction conferred by the Act of Congress, pursuant to constitutional authority, upon the equity powers of District Courts has been in any way modified or curtailed. Petitioner's argument must, therefore, descend from the realm of law to that of mere controversy. It argues not that the law has limited this jurisdiction of District Courts, but that it would be well for this Court now to engraft such a limitation and pronounce it as a matter of policy.

The Opinions of the District Court and of the Circuit Court of Appeals present an overwhelming array of authoritative decisions which, in discussing the federal equity jurisdiction, place it upon a broad and unrestricted plane. This jurisdiction,

derived as it is from the federal sovereignty, is of course immune from encroachment or restriction by the laws of any State. Petitioner concedes, as it must, the truth of this general principle. It argues, however, that this Court should now declare a limitation upon the federal equity jurisdiction in cases where a receivership is sought of a corporation which is quasi-public in character. Here, too, petitioner points to no federal statute which may afford even a preliminary justification for such an argument, and it concedes, as it must, that a long line of Federal authorities have recognized only a comprehensive and unlimited scope to the Federal jurisdiction.

In *Morrill* v. *American Reserve Bond Co., 151 Fed. 305, 313 (1907)*, Circuit Judge Sanborn said:

> "Wherever citizens of different states lawfully invoke the jurisdiction of the federal courts to determine controversies between them which involve the requisite amounts, they have the constitutional right to the conduct of that litigation by the methods, to the administration of the remedies, and to the determination of those controversies by the independent judgments of those courts; and no state, by conferring exclusive jurisdiction of such issues upon its own courts, by prescribing exclusive methods of commencing or of conducting litigation, by prohibiting the seizure of the subject of the litigation during its pendency, or by any other means, may lawfully strike down that right or take away the plenary power of the national courts to conduct the litigation, to administer their remedies, and in the exercise of their judicial discretion to control the possession of its subject-matter during its pendency in accordance with their established rules of practice, and finally to adjudicate the claims of the parties and to enforce their judgments (Citing many cases)."

To the same effect is *Leadville Coal Company* v. *McCreery, 141 U. S. 475, 477 (1891)*, where the Court said:

> "The Circuit Court takes its jurisdiction not from the State of Ohio, but from the United States; and the

extent of its jurisdiction is not determined by the laws of the State, but by those of the United States. Doubtless, while sitting in the State as a court of the United States, it accepts and gives effect to the laws of the State so far as they do not affect its jurisdiction and the rights of non-resident creditors. It nevertheless exercises powers independent of the laws of the State; and when, in pursuance of the jurisdiction conferred by the laws of the United States, it takes possession of the property of a defendant and proceeds to final decree, determining the rights of all parties to that property, its decree is not superseded and its jurisdiction ended by reason of subsequent proceedings in the courts of the State, looking to an administration of that property in accordance with the laws of the State. It would be an anomaly in legal proceedings if, after a court with full jurisdiction over property in its possession has finally determined all rights to that property, subsequent proceedings in a court of another jurisdiction could annul such decree, and disturb all rights once definitely determined. No such anomaly exists in the relative jurisdiction of state and Federal courts. The latter having once acquired full jurisdiction, and proceeded to a final determination, may rightfully proceed still further and to an execution of that decree, irrespective of any proceedings in the courts of the State."

We have already referred to the significant absence of any authorities in petitioner's Brief to support the distinction which it seeks to draw in the *jurisdiction* of the Federal Courts, as between suits against corporations generally and those against quasi-public corporations. Authority, however, is not wanting in which the general equity jurisdiction of Federal Courts was invoked and applied against quasi-public corporations.

In *New York Trust Co.* v. *Portsmouth & Exeter St. Railway Co., 192 Fed. 728 (1912)*, where a statute of New Hampshire provided that street railways were of public character and the owners could not discontinue them, nevertheless it was

held that where the Federal Court had properly acquired jurisdiction by reason of diversity of citizenship in a foreclosure suit, it could proceed with the foreclosure suit, and dispose of the assets of the company by sale.

In *Straine* v. *Bradford, 88 Fed. 571 (1898)*, where the Federal Court had properly acquired jurisdiction, it was held that even though a receiver was subsequently appointed by the state Court on petition of the Inspector of Finance of Vermont, this did not affect the Federal Court's jurisdiction and it would proceed with its case in the regular way.

A case clearly contrary to petitioner's argument is *Farrell* v. *Stoddard, Superintendent of Insurance of the State of New York, 1 F. (2d) 802 (1924)*. A non-resident, who was endeavoring to impress a trust against certain assets of the Niagara Insurance Company, which had been taken over by the Superintendent of Insurance of the State of New York, in accordance with its statutes, began his proceedings in the Federal Court of New York. The Superintendent of Insurance contested this, on the ground that the non-resident plaintiff must come into the state Court and that the Federal Court had no jurisdiction on the ground of comity because the *res* was already in the custody of the New York state Court in which the possession proceedings had been filed. There are several important principles set forth in this case, and we quote from the Opinion:

> "An examination of section 63 of the Insurance Law of the state of New York makes it clear that the superintendent of insurance is a public officer in the executive department of the state government, and that he still retains his character as a public officer when he acts as liquidator of insurance companies under the provisions of this statute. His power to act as custodian of the *res* comes alone from the statute. The judicial power cannot change or modify this statute, or affect his power in any respect whatever. True, the defendant must first apply to the court for an order to act as liquidator . . . Thereafter the defendant, as the

representative of the executive power, pays no heed to the court or its mandates. His chart is the statute under which he acts. . . .

. . . . . .

"No cases are cited by the defendant in support of his contention that this fund is in the custody of the state court. On the contrary, the defendant substantially conceded that the defendant superintendent of insurance is not a receiver or agent of the court, in his endeavor to have the courts of the state of New York decide that the superintendent of insurance is a representative of the sovereign power of the state, and could not be sued without the consent of the state. . . .

. . . . . .

"The defendant cannot well assert in the state court that he represents an independent branch of the sovereign power not subject to the court's control, and in this court assert he is the agent of the state court, and that his custody is the custody of that court. The fact that the defendant's contentions in either court do not determine the law of the case is not overlooked. . . .

"But the defendant also asserts that the Legislature has provided a method for the liquidation of the business, assets, and affairs of insurance companies by the defendant, to which all claimants must confine themselves, and that plaintiff has not done so. The statute in question does not assert that the method thus provided shall be exclusive, as do certain other statutes of the state. It is held on excellent authority that, where a remedy exists at common law and a remedial statute is directed at the same wrong, if such statute provides a larger or summary or more efficient remedy for the party aggrieved, but does not in terms or by necessary implication deprive the party injured of the remedy which existed at common law, the statutory remedy is considered as merely cumulative and the party injured may resort to either at his election. . . .

. . . . . .

"Even if the statute had in so many words expressed the intent to supersede the existing equitable and common-law

> rights, and to provide an exclusive method, it may well be doubted whether it would have any force or effect as to this plaintiff, a resident of Massachusetts, who is not subject to the jurisdiction of the laws of the State of New York as to his equitable or common-law rights, and has not sought the aid of the state courts. If the state of New York may, by legislative act, change the rights or remedies of a citizen of Massachusetts, it may change the rights or remedies of citizens of any other state and of all the states, and its power would, to the extent of rights arising from property existing in or illegally transferred to the state of New York, be equal to that of Congress. Such contention could not be maintained. In case of diversity of citizenship, one who elects to assert his equitable or common-law rights in a federal court cannot be deprived of them by the statutes of the state in which the federal court happens to exercise jurisdiction at the time. Morrill *v.* American Reserve Bond Co. (C. C.) 151 Fed. 305; Chicot County *v.* Sherwood, 148 U. S. 529, 13 S. Ct. 695, 37 L. Ed. 546. A federal court may not abdicate its duty or authority in any case in favor of another jurisdiction. Kline *v.* Burke Construction Co., 260 U. S. 226, 234, 43 S. Ct. 79, 67 L. Ed. 226, 24 A. L. R. 1077."

A similar case held that the Commissioner of Banking of Massachusetts, even though he took possession of a bank under the state statutes, is not such an official that the Federal Court cannot receive a suit from a non-resident plaintiff against him to establish a trust *ex maleficio* in connection with the funds in his hands: *Allen, Bank Commissioner* v. *U. S., 285 Fed. 678 (1923).*

In *Johnson* v. *Manhattan Ry. Co., 289 U. S. 479 (1933),* federal receivership of the street railway system of New York City, based on diversity of citizenship was sustained.

Authority is not wanting to illustrate the vitality of federal equity jurisdiction in suits against building and loan associations. The Opinion of Judge Welsh has set forth an imposing list of cases in which Federal Courts have appointed receivers for building and loan associations (R. 49-51).

Two decisions in the Circuit Court of Appeals for the Third Circuit long since established that federal jurisdictional authority was not to yield because of the character of the defendant.

In *Lyon* v. *McKeefrey*, *171 Fed. 381 (1909)*, diversity of citizenship was invoked by a resident of Ohio who filed a bill in the Federal Court for the appointment of receivers of a banking corporation organized under the laws of Pennsylvania. It was there pointed out that the Commonwealth of Pennsylvania, even under its own laws, had no exclusive jurisdiction over banking institutions.

In *O'Neil* v. *Welch*, *215 Fed. 201 (1917)*, the corporation involved was an insurance company chartered under the laws of Pennsylvania. There the district court upheld its jurisdiction to appoint receivers of such a quasi public corporation (*Welch* v. *Union Casualty Ins. Co.*, *238 Fed. 908 (1917)*), and the Circuit Court of Appeals, although deciding the case exclusively upon the question of priority in jurisdiction between the federal and the state Courts, uttered no disapproval of that view.

Not only is petitioner's argument contrary to the long standing decisions of the Federal Courts, but it is even at variance with the adjudication of the Supreme Court of Pennsylvania.

In *Jones* v. *Lincoln Savings & Trust Co.*, *222 Pa. 325, 71 A. 200 (1908)*, to which petitioner makes no reference, the court of Common Pleas of Philadelphia County appointed a receiver of a trust company upon a bill filed by a number of shareholders. Thereafter, at the instance of the Attorney General upon bill for dissolution under the former Act of February 11, 1895, P. L. 4, a receiver was appointed in the Dauphin County Court. The Attorney General sought to have this receiver supersede the Philadelphia receiver appointed on the stockholders' bill. The refusal of his prayer was affirmed by the Supreme Court of Pennsylvania. It probably was in consequence of this case that the Act of April 23, 1909, P. L. 167,

was passed providing that the appointment of a receiver "by any Court of this Commonwealth" should be cause for the superseding of that receiver on application by the Attorney General.

Finally, in *Mitchell* v. *Maurer*, 69 F. (2d) 233 (1934), a Federal receivership of a state insurance company was sustained notwithstanding the effort of the State Insurance Commissioner of California to be placed in possession of the business of the insurance company for the purposes of liquidation under the laws of that State. This court granted a writ of certiorari (*Mitchell* v. *Maurer*, 293 U. S. —— (1934)), but limited its review to the question of the validity of the appointment of ancillary receivers upon the petition of the primary receivers. In conformity with the decision in *McCandless* v. *Furland*, 293 U. S. —— (1934), the decision of the Circuit Court of Appeals in the Mitchell Case was reversed (293 U. S. —— (1934)). Nevertheless, we understand the limitation in the scope of the review granted by this Court to indicate that were it not for the lack of diversity of citizenship arising from the fact that the petition for ancillary receivers was filed by the primary receivers, the action of the Circuit Court of Appeals in the Mitchell Case would have been proper.

(d) *The Contract of subscription does not impair Federal jurisdiction.*

There remains for consideration the contention that the statutes of Pennsylvania relating to the supervision by the Secretary of Banking of institutions such as building and loan associations, form a comprehensive system of supervision and regulation which shareholders, by their subscriptions to stock in Pennsylvania corporations, agree to recognize. It is argued that in consequence of this alleged contract, the jurisdiction of Federal Courts is in all such cases wholly lost.

Petitioner refers to *McGarry* v. *Lentz*, 13 F. (2d) 51 (1926); *Cook* v. *Illinois Bankers' Life Assn.*, 46 F. (2d) 782

(1931); and *Haynes v. Fraternal Aid Union*, 31 F. (2d) 305 (1929), as laying down the rule that the contract of subscription between a shareholder and a corporation impliedly includes all provisions of the laws of the state of incorporation of his company. It is argued that in consequence of this rule Edwin B. Elson, who filed the bill for receivers in the present case, is bound by the laws of Pennsylvania relating to the supervision of building and loan associations by the Secretary of Banking and that these laws forbid him from invoking the jurisdiction of the Federal Court.

We need not dispute the entire line of argument which petitioner presses on this point, except that it is evident that the statutes to which petitioner refers have no such effect. If we assume that Mr. Elson became bound by the laws of Pennsylvania when he subscribed to his shares of stock in the Mortgage Building and Loan Association, an examination of the Banking Act of 1923 reveals, however, that the statute by which he was bound did not forbid him from invoking the jurisdiction of the Federal Court.

The law in force when the present proceeding arose was the Banking Act of 1923 (Act of June 15, 1923, P. L. 809, printed in full as an appendix to petitioner's Brief). In a number of instances petitioner's Brief ignores the plain provisions of that statute and states that a state Court is without authority to appoint receivers (See petitioner's Brief, pp. 10, 13, 14, 20, 31, 42). *This is not so.* The Courts of Pennsylvania had complete power to make unrestricted choice of receivers; the only limitation thereon was the subsequent one that the Secretary of Banking might, on account of the appointment of a receiver or for any other of many causes mentioned in the statute, take possession of an association, and upon so doing *supersede the receiver appointed by the state Court.* The provisions of the Banking Act of 1923 upon this subject follow:

> "The Secretary may . . . take possession of the business and property of any corporation or person subject to the supervision of the department, whenever it shall appear to him that such corporation or person:
>
> . . . . . .
>
> "IX. Is in the hands of a receiver appointed by any court, or in any bankruptcy proceeding, or of an assignee or trustee for creditors appointed by such corporation or person."

Section 22 provides for the taking of possession of the property of the corporation by the Secretary of Banking and the filing of a certified copy of a certificate of possession. It then proceeds:

> "From and after the filing of such certified copy in the office of the prothonotary, the secretary shall supersede any receiver, previously appointed by any court for, or any assignee or trustee for creditors appointed by, such corporation or person."

It is upon this very provision of subsection IX of Section 21 that petitioner bases its present petition (Paragraph 24, R. 26). It therefore argues that the appointment of receivers by the Federal Court was ground for the taking of possession and that the filing of a certificate of possession by the Secretary of Banking thereafter, because of such receivership, in law constitutes him a superseding receiver and therefore terminates the federal receivership. This whole argument, however, loses sight of the provision of Section 2 of the Act of 1923, which defines "Court" as:

> "The court of Common Pleas of the County where the banking house or other place of business of the corporation or person in question is located."

Accordingly, petitioner is not aided by the argument that Mr. Elson, in subscribing to the stock of the Mortgage Building and Loan Association, became bound by the laws of Penn-

sylvania. Those laws, we have seen, do not forbid him from invoking the jurisdiction of the Federal Court; they merely provide that if he or anyone else invoked the jurisdiction of the state court the Secretary of Banking *might, although he was not required to do so* by a certificate of possession, supersede such a receiver.

In short, the contract which petitioner argues Mr. Edson bound himself to by his stock subscription, did not bind him to refrain from seeking redress in either the federal or state Courts. The most it did was to make him subject to the state law by which a state receiver might be superseded by the Secretary of Banking in the discretion of that official. This distinction is clearly revealed in the cases cited by the petitioner. Thus in *Mercantile v. Lantz*, 13 F. (2d) 51 (D.C.) and in *Cook v. Liberty Bank, etc.*, Iowa, 50 F. (2d) 787 (1931), the state statute forbade application for receivership by anyone other than the Attorney General. The contract which the shareholder made, therefore, at most was a bartering away of his right to resort to other federal or state Courts for receivership.

On the other hand, in *Haynes v. Fraternal Aid Union*, 34 F. (2d) 455 (C.C.A.), also cited by petitioner, members of a fraternal insurance society filed a bill praying for the appointment of a receiver and for an accounting by certain officers who were alleged to have been guilty of misapplication of funds. The state statute prohibited receivership except on application of the Attorney General. The Court held that the shareholder was bound by this provision of the state law as a result of his contract of subscription, and that hence the prayer for receivership would be denied. *Nevertheless, the bill was sustained as to the prayer for accounting.* The Court said:

> "The state statute does not in terms provide for such an account [bill for accounting] against the officers by the Attorney General. It may be, by implication, he has such power. But there is no prohibition of the policy

holder maintaining such suit, and in the absence of such prohibition the statutory remedy is but cumulative (Citing authorities)."

The Pennsylvania statute makes no express provision with reference to resort to the *Federal Courts*. Even more, the state statute does not forbid resort to the state Court. It merely provides that the Secretary of Banking may, at his discretion, supersede a receiver appointed by a state Court. The effect of this is that no contract by Mr. Elson has any application to the present question. The present proceeding by the petitioner is not directed against Mr. Elson; his activity was terminated when the receivers were appointed. The petition is directed against the receivers who are the arm of the Federal Court. *They made no contract with the corporation and they are bound by none.*

It may therefore be concluded that the contract made by Mr. Elson with the association does not apply to a Federal Court, but merely to a state Court, and even then, does not forbid the institution of a suit for the appointment of receivers. The shareholder being permitted to secure the appointment of receivers in the Federal Court, he cannot by any contract determine the rights of the receivers so lawfully appointed.

There runs through petitioner's Brief the recurring error that no receiver may be appointed by a state Court. We have already pointed out that the only effect of the state law is to authorize the Secretary in his discretion to supersede a state receiver. That he need not do so is plain from the terms of the statute. And the practice under the statute indicates more conclusively than any argument what is the law and the policy pursued under it.

We may refer to at least one case in Pennsylvania, in Philadelphia County, in which, at the suit of a shareholder, receivers were appointed of a Pennsylvania building and loan association, likewise under the supervision of the Secretary of

Banking. Although the receiver was appointed more than two years ago, the Secretary of Banking has never filed a certificate of possession nor sought to supersede the state receiver. The state receiver is still in possession, liquidating the association, and has filed at least one partial account. The case we refer to is *Lindstrom v. U. S. National Building and Loan Association* (C. P. No. 1, Philadelphia County, June Term 1932, No. 8771, unreported).

Fresh evidence of the error of petitioner in this regard appears from the fact that the recent codification of the law, which of course is not applicable here, was drafted by the office of the Attorney General and clearly recognized that under the Banking Act of 1923 even the state Courts had the right to appoint receivers other than the Secretary of Banking.

The new law (Department of Banking Code of May 15, 1933, P. L. 565, Section 606), provides:

> "No Court shall appoint anyone but the Secretary [of Banking] as receiver of an institution. Whenever any court . . . shall determine that a receiver should be appointed . . . it shall appoint the Secretary as such receiver."

Even in this statute, "Court" is also defined as:

> "The Court of Common Pleas of the County in which the corporation or person has its principal or only place of business in this Commonwealth . . . " (Department of Banking Code, Section 2 A).

POINT II.

There was No Abuse of Discretion in the Appointment of Receivers.

(a) *The Secretary of Banking was not Exercising Jurisdiction over the Association.*

The main argument of petitioner is that the District Court abused its discretion in appointing the receivers and that this

abuse of discretion was so gross as to call for reversal upon appeal.

In order to measure the propriety of the action of the District Court, it is well to recall the circumstances under which it acted.

The Association was governed by the Banking Act of June 15, 1923, P. L. 809 (7 PS., Sections 1, *et seq.*). The present Department of Banking Code, approved May 15, 1933 (P. L. 565) and effective July 3, 1933, is a codification, restatement and alteration of the law. It was not in force, however, when the present proceedings were taken and hence is inapplicable here. An examination of the statutory law clearly reveals that prior to the Department of Banking Code of 1933 the method prescribed was loose and incomplete; and doubtless the Code and its companion Building and Loan Code of May 5, 1933 (P. L. 457), were enacted as a result of the deficiencies in the prior statutes.

How inadequate was the supposed system provided by the state law to which Petitioner refers is illustrated in a decision by the Supreme Court of Pennsylvania. In *Malis v. Homer Bldg. & Loan Assn., 314 Pa. 321, 171 A. 570, (1934)*, it was decided that prior to the Building and Loan Code of 1933 there was no legal foundation for voluntary liquidation of building and loan associations, and that accordingly a creditor was entitled to seize in execution any property of the association, despite the election of liquidating trustees. And it may be here observed that the almost universal practice of the Secretary of Banking in Philadelphia County has been not only to permit but to encourage the liquidation of associations through liquidating trustees.

An important reason for this practice on the part of the Secretary of Banking has been judicially noticed in another decision of the Supreme Court of Pennsylvania, which is not without significance here. In *Stone v. Schiller Bldg. & Loan Assn., 302 Pa. 544, 153 A. 758 (1931)*, an association with

a capital of $1,000,000 was liquidated by liquidating trustees, as the Opinion shows (p. 549), at the direction of the Secretary of Banking. Mr. Justice Kephart explained why this large association was not liquidated by the Secretary of Banking and why at his direction it was carried out in a manner which the subsequent opinion of the Supreme Court in the Malis Case showed was without legal authority. He said (p. 557):

> "The liquidation was ordered because, when done through statutory proceedings [by the Secretary of Banking], *there is too much waste to the shareholders.*"

Petitioner is driven to the anomalous argument that under the statute of Pennsylvania to which it points, the Secretary of Banking could have taken possession of the association as early as June 5, 1931, and yet failed to do so until the futile effort made after the appointment of receivers by the Federal Court. At the same time it argues that this inactivity and non-exercise of statutory power constitutes an exercise of "complete dominion over the affairs of Mortgage Building and Loan Association at the time complainant's bill was filed" (Petitioner's Brief, p. 38). From its own petition it appears that the Secretary of Banking did nothing until October 28, 1932, fifteen months later, when he requested a financial report, and on December 6, 1932, advised the officers of the Association that it was insolvent. This was all he did other than to suggest a method of operation, to select new counsel and a real estate advisor and to have the directors approve the various actions which he suggested. (Petition, pars. 10-12; R. 22).

He never exercised any authority or dominion over the association, never received one of its papers or documents into his possession or put them under his control, but permitted it to function as any other corporation in Pennsyl-

vania and as if it were a solvent association, leaving control entirely in the hands of its officers and directors.

As is well said by the Circuit Judge:

> "The association continued to go along and conduct business on this unstricted basis while insolvent or in an unsafe and unsound condition from June 5, 1931, until the Bill in this case was filed, February 9, 1933, when it was admittedly insolvent, with the interests of all persons who dealt with it or who were connected with it, in jeopardy" (R. 111).

What the Secretary should have done, and what alone would have constituted "full jurisdiction" over the liquidation of the association, was to take possession both because its condition was unsafe and unsound and because it was insolvent.

Much emphasis is placed upon the suggestions, letters or so-called orders from the Secretary of Banking. As shown by the District Judge, they constitute "mere admonitions" and do not "rise to the dignity of a restraining order" (R. 53). In fact they have no legal force except that their compliance may create an attitude of good-will, causing the Secretary of Banking to refrain from the exercise of his legal powers. This principle has been recognized in Pennsylvania. In *Blattenberger v. Sharswood Bldg. & Loan Assn., 19 Pa. D. & C. 447 (1933)*, the Department of Banking notified the association as to the manner in which it should conduct its business and placed it under "temporary restrictions," under which, *inter alia*, it was to pay no withdrawals and declare no maturities. The court held these letters merely directory and not binding, saying:

> "Section 20 of The Banking Act of June 15, 1923, P. L. 809, provided that 'Whenever it shall appear to the secretary that any corporation . . . is conducting business in an . . . unsafe manner, or that any such corporation has an impairment of capital, the secretary may issue an order, under his hand and seal of office, directing such corporation . . . to discontinue . . . such unauthorized or unsafe practices, or directing such corpo-

ration to make good, within a time of not more than sixty days after notice by the secretary, any impairment or deficiency of capital.' The letters from the secretary above referred to were not under his 'seal of office.' Indeed, they were not signed by him but by the assistant supervisor. They were not orders but merely requests. The defendant was not directed 'to make good . . . any impairment or deficiency of capital.' True, that of April 8, 1933, states that 'within sixty days you are to submit to this office a plan for rehabilitation of your affairs,' but submitting such a plan is not making good an 'impairment or deficiency of capital.' The letters referred to no 'unauthorized or unsafe practices,' but to the regular and proper acts of a building and loan association in the conduct of its business. Upon these the secretary was attempting to place 'temporary restrictions.' Under section 808 of the Building and Loan Code of May 5, 1933, P. L. 457, he now may do so by issuing an 'order of segregation,' but no such authority was vested in him prior to July 3, 1933, when that act became effective. It is therefore apparent that *the letters had no legal significance*, and that defendant should have credited plaintiff's payments on account of his shares of stock to the cancellation of his loan."

The letters in this case are similar in form and were equally unauthorized in law.

Had the Secretary been exercising full jurisdiction over the association, there would have been no power in the Nice Ball Bearing Company to proceed with execution (Banking Act of 1923, Secs. 29, 30, 7 PS.) and there accordingly would have been no need for the filing of the present Bill. It may be, as petitioner argues (Brief, p. 22), that "there is no charge in the bill of complaint that the Secretary of Banking . . . was guilty of neglect or delay in performing his duty." The answer to this assertion, however, is that the admitted facts proclaim his neglect. The Secretary's own petition reveals inactivity over a long period of time, rendering possible the consummation of the threatened attachment by Nice Ball Bearing Company and an unwilling-

ness to meet this threat which was only frustrated by the filing of the present Bill.

(b) *The District Court was Compelled to Exercise its Jurisdiction to Appoint Receivers.*

The circumstances already recited make it evident that it would rather have been an abuse of discretion if the District Judge had refused to appoint receivers. Under the unusual circumstances present in this case, the assertion that it was an abuse of discretion to appoint receivers is so extreme that to accept it as sound would be in effect to hold that there is no jurisdiction in any case to appoint receivers. It may therefore be understood why petitioner's argument on discretion is so indistinct from its argument on power. No stronger appeal to the discretion of a Court could be made than that presented by the plaintiff in this case. He appealed to the District Court under the Federal Constitution to extend to him as a citizen of New York its power of supervising and liquidating a Pennsylvania corporation through the instrumentality of a receivership in order to save the corporation in which he had a large financial interest from imminent destruction which the State authorities had long indicated they would not act to prevent.

Without further discussion, we submit that it is clear that petitioner cannot carry the heavy burden of showing a clear abuse of discretion, yet such is the burden upon it. In *Milwaukee and Minnesota Railroad Co.* v. *Howard, 131 U. S. Appdx. lxxxl (1866)*, this Court said:

> "The removal or appointment of a receiver, as we have heretofore said, rests in the sound discretion of the Court *and is not reviewable here.*"

In *Kingsport Press, Inc.* v. *Brief English Systems, Inc., 54 F. (2d) 497 (1931)*, (certiorari denied, *Owen* v. *Kingsport Press, 286 U. S. 545 (1932)*), the facts were so similar to those in the present case, that we set them forth at some length. The United States District Court for the Southern District of

New York appointed an equity receiver of the defendant. Thereupon a creditor of the defendant, who prior to the receivership had obtained a judgment and had allowed an appeal to be taken without the entry of security on the assurance of the defendant's then counsel that it was solvent, presented a petition to vacate the appointment of the receiver. The petitioner objected that the plaintiff's claim had not been reduced to judgment, that the suit was collusive and that its sole purpose was to prevent execution by petitioner.

On appeal Augustus N. Hand, of the Circuit Court of Appeals for the Second Circuit, after considering *Harkins* v. *Brundage*, *276 U. S. 36 (1928)*, cited by appellant as requiring the plaintiff to be a judgment creditor, said (pp. 500-1):

> "In most cases the estate can and should properly be administered in bankruptcy . . . In other words, we assume that the above dictum [in the Harkins Case] did not mean to proscribe the appointment of a receiver in equity for a railroad (which would not be subject to the Bankruptcy Act (11 U. S. C. A.)) or even for an industrial corporation, where it was made to appear that the corporation was likely to pay its creditors in full and to preserve its business through administration by a receiver, whereas the interests of general creditors would be greatly injured or destroyed if a single creditor were allowed to proceed with execution . . . Nor was the complainant here a mere dummy acting without risk of expense. On the contrary, it acted on its own behalf and through its regular attorneys and was vitally interested in not having the assets seized on execution by a judgment creditor who would get his claim paid in full while other creditors might have to go begging. In such circumstances, there can be no reason for holding that the judge abused his discretion in appointing a receiver or that the complainant was guilty of any fraud upon the judgment creditor, Owen, or upon the court. The judge, on the facts presented, adopted the only course that seemed to give the creditors of the defendant a chance to be paid in full or, even if they should not be paid in full, to be

treated equally . . . We should not interfere with the exercise of that discretion in the absence of proof of abuse. Sage *v.* Memphis, etc., Railroad Co., 125 U. S. 361, 8 S. Ct. 887, 31 L. Ed. 694; Folk *v.* United States (C. C. A.) 233 F. 177; Ward *v.* Central Trust Co. of Illinois (C. C. A. 252 F. 127; City Bond & Finance, Inc. *v.* Grant, (C. C. A.) 30 F. (2d) 671.

. . . . . .

"The contention that the appointment was obtained by collusion is based on a confusion of ideas. It seems to be thought that it was illegal for the defendant to inform the complainant that Owen was ready to issue execution or to take any steps that would facilitate a receivership. We can discover nothing illegal in this. Owen had no vested right to prevent other creditors from being paid if an administration of the property of the defendant through an equity receivership would produce such a result though after some inconvenience and delay to himself."

In *First National Bank of San Francisco v. Detroit Trust Co., 248 Fed. 10 (1918)*, it was said:

"It is to be observed that an appellate court will not reverse such an order as that which is here appealed from [the appointment of a receiver with authority to continue the business] unless it appears that the discretionary power of the court 'has been so improvidently and improperly exercised as to bring its action clearly within the meaning of the term "abuse of power."' Heinze *v.* Butte & Boston Consolidated Min. Co., 126 Fed. 1, 11, 61 C. C. A. 63, 73; United States Shipbuilding Co. *v.* Conklin, 126 Fed. 132, 60 C. C. A. 680; Briggs *v.* Neal, 120 Fed. 224, 56 C. C. A. 572."

This is the law in Pennsylvania.

In *Franklin National Bank v. Kennerly Coal & Coke Co., 300 Pa. 479, 150 A. 902 (1930)*, the Court states:

"The appointment of a receiver is a discretionary matter with the court below, and its action will not be disturbed unless there is a clear abuse of sound judicial discretion."

As a matter of law, such an appointment was not appealable in the Federal Courts until the passage of the Act of April 14, 1906, 34 Stat. at L. 116 (now contained in Sec. 129 of the Judicial Code, 28 U. S. C. A. 227). See *Loveland's Appellate Federal Jurisdiction, Secs. 187, 193.*

Not only does petitioner carry a heavy burden in seeking upon appeal to convict the Court below of an abuse of discretion, but it carries the additional burden of showing that the appellate Court itself, which sustained the Court below, likewise was guilty of an abuse of discretion. We submit that petitioner's case falls far short of meeting this twice heavy burden.

A number of authorities have been cited with respect to the exercise of discretion. Petitioner seems to place great reliance upon *Port Newark National Bank of Newark* v. *Waldron*, 46 F. (2d) 296 (1930). The Opinion in that case was written by Judge Buffington, who likewise sat in the present case and joined in the decision which petitioner here attacks. That case does not involve the exercise of discretion by a Federal Court where the rights or duties of state officials are involved. Rather does it concern the appointment of receivers of a *national bank* by a Federal Court where the federal Comptroller of the Currency has appointed a receiver. As was said by Judge Buffington:

> "This is not a conflict of two courts of coordinate jurisdiction, but is one between the judicial and the executive arm of the [same] sovereignty."

It is of little avail, however, to argue at length that in a case of such inactivity on the part of the state official and such pressing danger threatened by a judgment shareholder, the exercise of conceded jurisdiction was so arbitrary, that having escaped condemnation upon appeal, this Court should now interfere.

POINT III.

Conclusion.

It is argued by petitioner that the decision of the Circuit Court of Appeals in effect assists a building and loan association to escape the jurisdiction and laws of the state creating it. This argument comes far too late for it has found organic expression in the Constitution of the United States in cases of diversity of citizenship (Art. III, Sec. 2). Nowhere in the Record can be found a single fact which supports the argument that to permit liquidation of a building and loan association under the jurisdiction of a federal Court will result in the destruction of its assets and the ruin of its shareholders. The language of the Supreme Court of Pennsylvania in the Stone Case, which we have already quoted, eloquently answers this argument. Surely it would be a novel thing for this Court to judicially notice as true an argument which on its face must prove unsound and a reflection upon the Federal Courts. The petitioner, however, should have descended from such a generality to this particular case. The conduct of the state officials can in no way be justified and that unjustifiable conduct alone made necessary and possible the appointment of federal receivers. The proper method of avoiding federal receivership of a building and loan association is not to destroy a constitutional jurisdiction but for state officials to execute the laws. If, under the laws existing when these proceedings arose, the Secretary of Banking had taken possession of unsafe and unsound or insolvent associations there could be no federal receivership. If his neglect of the power conferred upon him has resulted in administration through some other agency, he cannot complain.

The entire fallacy of petitioner's argument rests in its failure to recognize that under the Act of 1923 and similar legislation, the Secretary's power of supervision was not an exercise of possession or jurisdiction over building and loan

associations. It is quite probable that the Building and Loan Code of 1933, which provides for Orders of Segregation (Section 808) is legislative recognition of the prior error entertained by the Department of Banking. Under the new law the Secretary of Banking is given intermediate jurisdiction over associations, even short of the taking of possession. His orders in such cases may not be, as heretofore, mere words of advice which in practice an insolvent association would feel impelled to follow but which a sound and solvent association might legally defy. If this be true, then such intermediate orders, made in the future, may prevent federal receivership in all such cases because the *res* will have been already in the possession of the state.

But it is well that non-residents should know that the jurisdiction of Federal Courts is still available to them. To use the illustration of a bank or trust company, which petitioner seems to believe is so conclusive in its favor, is there any public policy which should destroy the jurisdiction of Federal Courts in a case where the state agency negligently refuses to take possession of a bank or trust company which for almost two years has been insolvent? If the state authorities should for any reason be unwilling for two years to close the doors of an insolvent bank, it is well that Federal Courts have the power to intervene and do so themselves.

The plaintiff in this case is admittedly a non-resident and had invested $31,200. in the association which the state agencies did not properly protect. Vigilance, activity and performance of duty by the Secretary of Banking would have rendered a federal receivership unnecessary. Had he taken possession it would have rendered unnecessary the exercise of constraint upon the association in the choice of its solicitors and real estate agents by the threat of possession.

We may also call attention to Equity Rule 37 which provides:

> "Anyone claiming an interest in the litigation may at any time be permitted to assert his right by intervention, but the intervention shall be in subordination to, and in recognition of, the propriety of the main proceeding."

This rule has been interpreted in many cases unfavorably to petitioner here. Among these cases may be mentioned *Board of Drainage Com'rs.* v. *Lafayette South Side Bank of St. Louis, 27 F. (2d) 286 (1928).*

It is submitted that this case involves, not high questions of public policy, but a very common illustration of an attempt to alter well established law to justify administrative inactivity and neglect.

Respectfully submitted,

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